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COMMENTS

LIABILITY INSURANCE COVERAGE FOR SUPERFUND CLAIMS: A MODEST PROPOSAL

I. INTRODUCTION

In 1980, Congress enacted the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA)¹ to establish a framework for the efficient cleanup of hazardous waste sites in the United States. One of the fundamental principles underlying this statutory scheme known as "Superfund" is that, to the extent possible, those responsible for releases of hazardous substances will pay the costs of cleanup. The result of this policy has been a veritable tidal wave of litigation in the state and federal courts since 1981, with potentially responsible persons (PRPs) seeking shelter from possible exposure to multi-million dollar liability claims under CERCLA's infamous section 107.²

The spectre of such litigation is grotesque, indeed. Despite the legislative attempt to expedite cleanup cost recovery by a strict, joint and several liability system with only limited defenses,³ litigation under CERCLA has been notoriously slow-moving and extraordinarily expensive.⁴ In fact, some have noted that litigation costs could actually exceed the costs of the cleanups themselves.⁵ For this reason, PRPs have eagerly sought escape from the Superfund liability crunch through various financial responsibility means.

One financial option is filing a claim under a commercial liability insurance policy. The most common such policy for business and industry during

1. Pub. L. No. 96-510, 94 Stat. 2767 (1980) (codified as amended at 42 U.S.C. §§ 9601-9657 (1982)).

2. See generally Comment, *Personal Liability for Hazardous Waste Cleanup: An Examination of CERCLA § 107*, 13 B.C. ENVTL. AFFAIRS L. REV. 643 (1987).

3. See generally *United States v. Northeastern Pharmaceutical & Chem. Co.*, 579 F. Supp. 823 (W.D. Mo. 1984); Korhonen & Smith, *CERCLA Defendants*, 31 WASH. U.J. URB. & CONTEMP. L. 289 (1987); Warsbaur & Stansel, *Civil, Governmental, and Criminal Obligations and Liabilities for Hazardous Waste*, 14 TORT & INS. L.J. 37 (1986); Comment, *supra* note 2.

4. Comment, *Developments in the Law: Toxic Waste Litigation*, 99 HARV. L. REV. 1458, 1494 (1986); see also Whitehead, *Hazardous Waste and Toxic Torts: Handling Litigation and Insurance Coverage*, 51 INS. COUNS. J. 218 (1984).

5. Atkeson, *Superfund Amendments and Reauthorization Act: An Annotated Legislative History*, 16 ENVTL. L. REP. 10360, 10368-69 n.80 (1986).

the 1960s and 1970s was the Comprehensive General Liability (CGL) policy.⁶ The presence of CGLs has resulted in a second wave of litigation, this time pitting PRPs against their insurers in declaratory judgment actions to determine the rights and liabilities of the parties under these policies.⁷ The lawsuits have forced federal and state courts to consider a number of creative arguments surrounding the difficult legal issue of whether coverage exists in the first instance, and the still more vexing public policy consideration of whether coverage *ought* to exist.⁸ It is clear that the CERCLA cleanup scheme cannot succeed without recovering the costs which are expended to fund superfund response activities. Thus, the question becomes to what extent, if any, those costs should be allocated through traditional risk management processes.

II. THE PLIGHT OF XYZ CORPORATION

To facilitate this discussion, consider the following hypothetical:⁹

XYZ Corp. is a small, closely-held Missouri corporation in the business of manufacturing widgets. From 1965 through 1980, XYZ engaged in widget manufacturing at a small plant in Pleasant Valley, Missouri.

In the regular course of widget manufacturing, several chemical solvents are used as cleansing agents. XYZ stored these chemicals in metal drums while operating at Pleasant Valley, and disposed of waste chemicals by burying the drums on the site. Also, during the course of the cleansing process, small amounts of the chemicals spilled and escaped through cracks in the floor. In 1980, XYZ ceased operations at Pleasant Valley.¹⁰

In 1982, the Environmental Protection Agency discovered dangerously high levels of the hazardous substances used by XYZ in soil samples taken from the area around the the Pleasant Valley plant.¹¹ Additionally, in 1984 a monitoring well placed on the site revealed toxic concentrations of certain met-

6. For a history of the CGL, see Hourihan, *Insurance Coverage for Environmental Damage Claims*, 15 FORUM 551 (1980); R. LONG, *The Law of Liability Insurance*, 3 app. at 58 (1980). See generally *American Home Prods. v. Liberty Mut. Ins. Co.*, 565 F. Supp. 1485, 1500-03 (S.D.N.Y. 1983), *aff'd as modified*, 748 F.2d 760 (2d Cir. 1984).

7. See generally Comment, *The Pollution Liability Insurance "Crisis"*, 15 CAP. U.L. REV. 677 (1986); Note, *The Applicability of Liability Insurance in Hazardous Waste Disposal*, 57 S. CAL. L. REV. 745 (1984).

8. See *infra* notes 99-109 and accompanying text.

9. The persons and events depicted in this hypothetical are entirely fictional; any similarity to actual persons or events is purely coincidental.

10. 42 U.S.C. § 9601(22) (1982) defines "release" of hazardous substances as "any spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, dumping, or disposing into the environment (including the abandonment or discarding of barrels, containers, or other closed receptacles containing any hazardous substance, pollutant or contaminant). . . ."

11. 42 U.S.C. § 9601(14)(C) (1982) defines "hazardous substances" by means of a cross-reference to the Resource Conservation and Recovery Act (RCRA), 42 U.S.C. § 6921 (1982).

als in area groundwater. Based on this research, E.P.A. ordered an immediate Removal Action¹² and undertook a Remedial Investigation¹³ and Feasibility Study concerning long-term cleanup of the Pleasant Valley site.

XYZ has been served with a complaint by the United States government seeking \$1 million in Response Costs¹⁴ for cleanup of the Pleasant Valley site, as well as a declaration of liability for future response costs and natural resources damage.¹⁵

During the period of alleged contamination, XYZ was covered by the following liability insurance policies:

- 1968-1970 Good Faith Mutual, \$1 million limit.
- 1970-1971 Good Hands Ins. Co., \$2 million limit.
- 1971-1976 Joe's Ins. Co., \$1 million primary,
\$2 million excess limit.
- 1976-1978 Condition Precedent Casualty, \$1 million
primary; Nice Guys Mutual, \$1 million
excess.
- 1978-1980 Good Hands, \$3 million "umbrella"

After XYZ filed its notices of claims, each of these insurers, as have most in similar situations, decided to "run for cover rather than coverage."¹⁶ XYZ's registered agent received a second summons and complaint, from Good Hands, naming XYZ and the other insurers as parties defendant, seeking a declaration of noncoverage under the policies it issued to XYZ. The stage is set for a typical declaratory judgment battle over the applicability of CGL insurance policies to hazardous waste cleanup claims.¹⁷

12. 42 U.S.C. § 9601(23) (1982) defines "removal" as "the cleanup or removal of released hazardous substances from the environment, . . . such actions as may be necessary to monitor, assess, and evaluate the release or threat of release of hazardous substances, the disposal of removed material. . . ."

13. 42 U.S.C. § 9601(24) (1982) defines "remedial action" as "those actions consistent with permanent remedy taken instead of or in addition to removal actions in the event of a release or threatened release of a hazardous substance into the environment . . . [to prevent] substantial danger to present or future public health or welfare. . . ."

14. 42 U.S.C. § 9601(25) (1982). Judicial construction of this term has been very broad. *United States v. Northeastern Pharmaceutical & Chem. Co.*, 810 F.2d 726, 732 (8th Cir. 1986), *cert. denied*, 108 S. Ct. 146 (1987); *see also United States v. Northeastern Pharmaceutical & Chem. Co.*, 579 F. Supp. 823, 850 (W.D. Mo. 1984).

15. 42 U.S.C. § 9607(a)(4)(C) (1982) concerns liability for damage to natural resources. Future response costs are recoverable either by the government, *United States v. Wade*, 577 F. Supp. 1326 (E.D. Pa. 1983), or by private parties, *United States v. Conservation Chem. Co.*, 628 F. Supp. 391 (W.D. Mo. 1985).

16. *Sandoz, Inc. v. Employers Liab. Assurance Corp.*, 554 F. Supp. 275, 278 (D.N.J. 1983).

17. Note that the scenario outlined in this hypothetical fairly represents that occurring in reported cases. *See, e.g., Mraz v. Canadian Universal Ins. Co.*, 804 F.2d 1325 (4th Cir. 1986); *Fireman's Fund Ins. Co. v. Ex-Cell-O Corp.*, 662 F. Supp. 71 (E.D.

III. OVERVIEW OF INSURANCE CONCEPTS

In order to understand the issues facing the district court in the fictional *Good Hands v. XYZ* litigation, it is necessary to discuss some basic concepts of insurance law. These "canons of construction" are essential in understanding the interaction between the public policies relevant in hazardous waste—liability insurance cases.

Initially, it should be noted that insurance policies are, in the most fundamental sense, contracts. They are subject to the same rules of construction as ordinary contracts, at least in the first instance. As with all contracts, language in insurance policies will be given "its ordinary meaning and effect" in the absence of ambiguity.¹⁸

The unique feature of insurance contracts, however, is their "adhesive" character; that is, insurance policies are issued to an insured on a "take it or leave it" basis.¹⁹ This lack of meaningful bargaining over important policy terms makes it less difficult for courts to find the requisite "ambiguity" to trigger the opportunity for judicial construction. It is with this in mind that special scrutiny is given to terms in insurance contracts by which an insurer seeks to avoid coverage. The oft-mentioned canons include construction of policy terms in the manner which "maximizes coverage"²⁰; construction of ambiguous terms strongly against the insurer²¹; and the applicability of these rules even when the insured is a commercial entity, presumably sophisticated in contract negotiations.²²

These rules of construction are of paramount importance when discussing exclusionary clauses, or conditions subsequent, designed to avoid coverage in instances where it would otherwise exist. Such restrictions are given the strictest judicial scrutiny.²³ Moreover, the burden rests with the insurer to demonstrate the factual applicability of the clauses,²⁴ and to do so "clearly and unambiguously."²⁵ As one court has observed:

Mich. 1987); *Fischer & Porter Co. v. Liberty Mut. Ins. Co.*, 656 F. Supp. 132 (E.D. Pa. 1986).

18. *Pearce v. General Am. Life Ins. Co.*, 637 F.2d 536, 539 (8th Cir. 1980).

19. *Estrin Constr. Co. v. Aetna Casualty & Sur. Co.*, 612 S.W.2d 413, 418-19 (Mo. Ct. App. 1981).

20. *Continental Ins. Cos. v. Northeastern Pharmaceutical & Chem. Co.*, 811 F.2d 1180, 1192 n.29 (8th Cir. 1987); *Bellamy v. Pacific Mut. Life Ins. Co.*, 651 S.W.2d 490, 496 (Mo. 1983) (en banc).

21. *Missouri Terrazzo Co. v. Iowa Nat'l Mut. Ins. Co.*, 566 F. Supp. 546, 552 (E.D. Mo. 1983) (citing *Citizens Ins. Co. v. Kansas City Commercial Cartage*, 611 S.W.2d 302, 307 (Mo. Ct. App. 1980)).

22. See, e.g., *Missouri Terrazzo Co. v. Iowa Nat'l Mut. Ins. Co.*, 566 F. Supp. 546 (E.D. Mo. 1983).

23. *McMichael v. American Ins. Co.*, 351 F.2d 665, 669 (8th Cir. 1965).

24. *Michigan Mut. Ins. Co. v. Stallings*, 523 S.W.2d 539, 545 (Mo. Ct. App. 1975).

25. *Insurance Co. of N. America v. General Aviation Supply Co.*, 283 F.2d 590 (8th Cir. 1960).

[W]henver the insurer wishes to exclude certain coverage from its policy obligations, it must do so "in clear and unmistakable language." Any such exclusions or exceptions from policy coverage "must be specific and clear in order to be enforced. They are . . . to be accorded a strict and narrow construction." . . . the burden is upon the insurer to prove that the exclusion from liability coverage applies.²⁶

IV. POLICY PROVISIONS OF THE CGL

Assume that each of the CGL policies covering XYZ during the period of alleged contamination contained the following provisions:²⁷

1. *Coverage*. Insurer agrees to pay, on behalf of XYZ, all sums which XYZ becomes legally obligated to pay as damages because of bodily injury or property damage, to which this insurance applies, caused by an "occurrence."

2. *"Occurrence" definition*. Occurrence means an accident, including continuous or repeated exposure to conditions, injury or property damage neither expected nor intended by XYZ.

3. *"Property Damage" definition*. Property damage means physical injury or destruction of tangible property which occurs during the policy period, including the loss of use thereof at anytime resulting therefrom.

4. *Pollution Exclusion*. This insurance does not apply to bodily injury or property damage arising out of the discharge, dispersal, release or escape of smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gases, waste materials or other contaminants or pollutants into the environment; but this exclusion does not apply if such pollution is "sudden and accidental."

The Good Hands Complaint asserts all four policy provisions as defenses to coverage of XYZ's liability in the *United States v. XYZ* cost recovery suit. Specifically, Good Hands contends that the release at the Pleasant Valley site was not an "occurrence" within the policy definition of that term; that, even if it was an occurrence, it did not result in "property damage" which occurred "within the policy period;" that, even if "property damage" occurred, response costs are not "damages" which the insured may become "legally obligated to pay;" and, finally, even if all conditions precedent to coverage arguably exist, the pollution exclusion is applicable and precludes coverage. Each of these issues has been the subject of much litigation in the hazardous waste - liability insurance context.

26. National Grange Mut. Ins. Co. v. Continental Casualty Ins. Co., 650 F. Supp. 1404, 1408 (S.D.N.Y. 1986) (citations omitted).

27. The policy provisions described are fictional; they are essentially paraphrases of the amalgam of such provisions discussed in the reported cases. See, e.g., National Grange Mut. Ins. Co. v. Continental Casualty Ins. Co., 650 F. Supp. 1404, 1408-09 (S.D.N.Y. 1986); Mraz v. American Universal Ins. Co., 616 F. Supp. 1173, 1177-78 (D. Md. 1985); Continental Ins. Cos. v. Northeastern Pharmaceutical & Chem. Co., 24 Env't Rep. Cas. (BNA) 1868, 1871 (W.D. Mo. 1985).

V. JUDICIAL TREATMENT OF THE INSURANCE ISSUES

A. Was there an "Occurrence?"

The first issue facing the district court in *Good Hands v. XYZ* is whether the release²⁸ of hazardous substances at Pleasant Valley was an "occurrence" within the policy definition of that term. Stated differently, the court must determine whether the escape into the environment of TCE was a phenomenon "neither expected nor intended" by XYZ.

It is important to note that the presence of an occurrence is a condition precedent to coverage.²⁹ If the events in question do not amount to an "occurrence" as defined in the policy, the loss is not covered regardless of the merits of the other issues in the case. Because the issue is one of coverage, XYZ bears the burden of proving that the release of cleansing chemicals was an occurrence as defined in the insurance policy.³⁰

At first blush, this may appear difficult. After all, the storage, use and disposal of toxic chemicals by XYZ at the Pleasant Valley site were both "expected and intended." In other contexts, the element of intent is fulfilled if the actor intended the *act* in question, regardless of his knowledge of the *results* that followed.³¹ Applying this standard, XYZ could not fit the release of contaminants within the occurrence definition merely because the harmful consequences of the handling of chemical solvents at the plant were not known at the time of the activity; rather, the intentional, expected use and disposal of hazardous substances would be sufficient to disqualify the leaks from the occurrence classification, to prevent the existence of the condition precedent, and thus to defeat coverage.

At least one court has so held. In *American States Insurance Co. v. Maryland Casualty Co.*,³² the district court reasoned that a release of hazardous substances could not be said to have resulted in an "accident" where the insured's "regular and continuous" activity of illegally dumping toxic waste was the cause.³³ The breadth of the court's holding is questionable, however, because of the *illegality* of the insured's activity. The court's reliance on Long's treatise on liability insurance³⁴ is significant. Long suggests that a narrow application of CGL coverage for hazardous waste cases is appropriate only where the insured is an "active polluter," *i.e.*, one who actually intends the harmful results of his activity.³⁵ Thus, absent illegality of the insured's conduct, it is

28. "Release" is defined *supra* note 10.

29. R. KEETON, INSURANCE LAW: BASIC TEXT § 6.5(b), at 379 (1971).

30. *Id.*; *United States v. Conservation Chem. Co.*, 653 F. Supp. 152 (W.D. Mo. 1986).

31. This is true of intentional torts, for example. See W. PROSSER, PROSSER AND KEETON ON TORTS § 8 (5th ed. 1984).

32. 587 F. Supp. 1549 (E.D. Mich. 1984).

33. *Id.*

34. See *supra* note 6.

35. *Id.* For a discussion of the pollution exclusion, see *infra* notes 70-98 and ac-

doubtful that *American States* provides much precedent for taking a narrow view of the occurrence definition in the hazardous waste context. In fact, in a recent decision, the same district court held that a release of hazardous substances *could* constitute an occurrence, distinguishing *American States* on that basis.³⁶

This appears to be the view of the overwhelming majority of courts. Most agree that, with respect to the insured's expectations or intentions, the focus should be the *result* rather than the *act*. That is, if the contamination was beyond the contemplation of the insured at the time of the conduct in question, the release constitutes an occurrence despite the concededly intentional nature of the acts of disposal.³⁷ This seems to be the better view, and one which is consistent with traditional notions of liability insurance coverage.³⁸

Thus, it appears that XYZ will be able to overcome Good Hands' first policy defense if it can be shown that XYZ neither expected nor intended the damage caused by the release at the Pleasant Valley site. Assuming that both the fact and the extent of the contamination of the soil and groundwater was neither expected nor intended by XYZ at the time of the contamination at the site, the subsequent release was an occurrence within the policy definition of that term.

B. Did the "Release" cause "Property Damage?"

The next issue before the court is whether the release resulted in "property damage within the policy period." This, like the presence of an occurrence, is a condition precedent to coverage and places the burden of proof on XYZ. Absent a showing that XYZ's liability for cleanup costs established in the *United States v. XYZ* cost recovery case represents "damages" resulting from property damage within the applicable period of policy coverage, the insurance policies do not cover the cost recovery claim.

This issue actually involves two related subissues: first, whether cleanup costs constitute property damages "within the policy period," despite the fact that they are not incurred until long after the contamination; and second, whether cleanup costs represent "damages" as that term is used in the coverage provision of the CGL. Unlike the "occurrence" issue, insurers recently have achieved success with these policy defenses.

companying text.

36. See *Fireman's Fund Ins. Co. v. Ex-Cell-O Corp.*, 662 F. Supp. 71 (E.D. Mich. 1987). But see *Grant-Southern Iron & Metal Co. v. CNA Ins. Co.*, 26 Env't Rep. Cas. (BNA) 1668 (E.D. Mich. 1986), where the eastern district court found in favor of the insurer on the basis of the pollution exclusion, discussed *infra* notes 79-98 and accompanying text.

37. *Continental Ins. Cos. v. Northeastern Pharmaceutical & Chem. Co.*, 811 F.2d 1180, 1183 n.5 (8th Cir. 1987).

38. Chesler, Rodburg & Smith, *Patterns of Judicial Interpretation of Insurance Coverage for Hazardous Waste Site Liability*, 18 RUTGERS L.J. 9 (1986); see also *White v. Smith*, 440 S.W.2d 497, 507-08 (Mo. Ct. App. 1969).

1. When does the "property damage" occur?

The two cases at odds on this issue are *Continental Insurance Cos. v. Northeastern Pharmacy & Chemical Co.*³⁹ and *Mraz v. Canadian Universal Insurance Co.*⁴⁰ In *Mraz*, the Fourth Circuit Court of Appeals gave the term "property damage within the policy period" a very narrow construction, holding that "in hazardous waste burial cases such as this one, the occurrence is judged by the time at which the leakage and damage are first discovered. . . . Nothing in the complaint indicates that the release was discovered any earlier than 1981, over eleven years after Canadian Universal went off the risk."⁴¹

The Fourth Circuit's reasoning parallels that of District Judge Clark in *Continental Insurance*. In granting the insurer's motion for summary judgment, Judge Clark stated:

Although the complaint suggests that the wrongful and negligent act did occur during the policy periods, there is no allegation that the State of Missouri or the United States incurred any loss or damage during this same policy period. It was not until the governmental entities incurred remedial or removal costs that they sustained a loss which was compensable. . . . Accordingly, since there was no damage or loss incurred by the governmental entities until after the policy period effective dates, there was not an occurrence giving rise to the insurer's liability for their losses.⁴²

Under the strict formulation prescribed by the Fourth Circuit and Judge Clark, XYZ will be unable to demonstrate the applicability of the Good Hands policy or any of the other CGLs in effect during the period of alleged contamination. This is because the property damage in question was not *discovered* until long after the policies lapsed. By focusing on the point at which the contamination is discovered and response costs are incurred, this narrow view would deny liability coverage for virtually all hazardous waste cleanup cases. The time of the factual occurrence - that is, the insured's activity - ordinarily predates the discovery of the damage by many years. Moreover, since the "property damage" in hazardous waste cases is predominantly by its very nature *latent* - soil and groundwater contamination, for instance - focusing on the time of discovery and cleanup will invariably lead to avoidance of coverage in hazardous waste cases.

39. 24 Env't Rep. Cas. (BNA) 1868 (W.D. Mo. 1985), *rev'd in part and remanded*, 811 F.2d 1180 (8th Cir. 1987), *aff'd in part and rev'd in part*, 842 F.2d 977 (8th Cir. 1988) (en banc). For purposes of this discussion, the initial Eighth Circuit decision will be referred to as the "Panel Opinion".

40. 616 F. Supp. 1173 (D. Md. 1985), *rev'd*, 804 F.2d 1325 (4th Cir. 1986).

41. *Mraz*, 804 F.2d at 1328 (4th Cir. 1986). Note that the Fourth Circuit opinion links the "occurrence" and "property damage" issues together; the case appears to hold that there was no occurrence, but actually it holds that there was no occurrence because no property damage was sustained during the policy period. *Id.*

42. *Continental Ins.*, 24 Env't Rep. Cas. (BNA) at 1873 (W.D. Mo. 1985). Note that, like the Fourth Circuit, Judge Clark links the occurrence and property damage - policy period issues.

This result proved too much for the Eighth Circuit. Taking a different analytical approach in the appeal from Judge Clark's decision, that court found that claims for environmental contamination could constitute "property damage" in some instances, even when the damage remained undiscovered until after the policies lapsed.⁴³ The court noted that the issue turned on the operative point in question: "environmental damage occurs at the moment the hazardous wastes are improperly released into the environment . . . a liability policy in effect at the time this damage is caused provides coverage for the subsequently incurred costs of cleaning up the wastes."⁴⁴ On rehearing, the court en banc upheld this portion of the panel opinion.⁴⁵

2. Are "response costs" "damages?"

The other issue is whether the incurrence of response costs by the state and federal governments constitute "damages," as that term is used in the coverage provision of the CGLs. The *Mraz* court found that they did not, noting that "while the complaint does allege that property damage occurred, there are no allegations that *plaintiffs* sustained any property damage Response costs are not themselves property damages Instead, response costs are an economic loss. Therefore, the *Bissell* complaint does not allege a loss of property damage."⁴⁶

Then, in a recent decision, the Fourth Circuit went one step further in its rejection of liability coverage for CERCLA response costs. In *Maryland Casualty Co. v. Armco, Inc.*,⁴⁷ that court held that response costs are not legal "damages," but rather are restitutionary amounts awarded in equity; as such, a CERCLA cost recovery claim is "not a suit for damages against which [the insurer] must defend and indemnify."⁴⁸

The Fourth Circuit construed the term "damages" in the CGL coverage section as a word of limitation, positing that "if the term 'damages' is given the broad, boundless connotations sought by the appellant, then the term 'damages' in the contract . . . would become mere surplusage, because any obligation to pay would be covered. The limitation implied by use of the phrase 'to pay as damages' would be obliterated."⁴⁹

The question of whether CERCLA cleanup costs are legal damages gave the Eighth Circuit considerably more difficulty in the *Continental Insurance* litigation. In the panel opinion, the majority of the court, over Judge McMillian's dissent, disposed of this issue by relying on a line of United States Supreme Court cases holding that the federal and state governments have a le-

43. *Continental Ins.*, 842 F.2d at 983.

44. *Continental Ins.*, 811 F.2d at 1189 (footnotes omitted).

45. *Continental Ins.*, 842 F.2d at 983-87.

46. *Mraz*, 804 F.2d at 1329 (4th Cir. 1986), *cert. denied*, 108 S. Ct. 703 (1988).

47. 822 F.2d 1348 (4th Cir. 1987).

48. *Id.* at 1351.

49. *Id.* at 1352.

gally cognizable interest in all property within their territorial borders⁵⁰ and hold that property in "public trust" for the common good. To this extent, contamination of any soil or groundwater constitutes an infliction of damage to property of those governmental entities.⁵¹ Since the contamination in fact occurred while the policies were in effect, although admittedly undiscovered at that time, exposure of the publicly-held environment to the contaminants also "exposed" the liability insurance policies in effect at the time to damage claims.

Further, the Eighth Circuit panel found that the CGLs, by their very terms, contemplated coverage of response costs. It pointed to the language of the coverage section, which says that the insurer will pay not only "property damage" claims, but *all sums* for which the insured becomes liable "as damages *because of* property damage which occurs within the policy period."⁵² The panel majority concluded that the policy would cover the response costs because the cleanup costs sought by the governmental entities in the underlying litigation constituted "compensatory damages" which flowed directly from property damage that occurred during the policy period - strictly speaking, the moment at which the hazardous substances were exposed to the environment.⁵³

On rehearing en banc, however, the court changed its mind. Judge McMillian, this time writing for the majority, agreed with the *Maryland Casualty* holding that response costs are restitutionary amounts awarded in equity, rather than legal "damages," and therefore are not envisaged by the coverage provision of the CGLs.⁵⁴ The court stated that "in the insurance context . . . the term 'damages' is not ambiguous, and the plain meaning of the term damages . . . refers to legal damages and does not include equitable monetary relief."⁵⁵ In so holding, the majority of the Eighth Circuit en banc eliminated the "circuit split" which had existed previously.

The original Eighth Circuit view, as expressed by the majority in the panel opinion, appears to be the most consistent with the language of the CGL policies and common sense. Moreover, both *Maryland Casualty* and the Eighth Circuit's en banc opinion ignore the long-standing "canons of construction" of insurance contracts, the latter case satisfied to base its holding on a conclusory statement of "black letter insurance law."⁵⁶ The earlier Eighth Circuit panel decision does a better job than the second in applying the boilerplate CGL language to an extremely difficult factual setting with peculiar considerations. As Judge Heaney noted in the dissent:

50. *Id.* at 1185-87.

51. *Cf. Illinois v. City of Milwaukee*, 406 U.S. 91 (1972) (applying the theory to the federal government); *Georgia v. Tennessee Copper Co.*, 207 U.S. 230 (1907).

52. *Continental Ins.*, 811 F.2d at 1188-89.

53. *Id.*

54. *Continental Ins.*, 842 F.2d at 987.

55. *Id.* at 985.

56. *Id.* at 986. This reference was criticized by the dissent. *Id.* at 989 n.1 (Heaney, J., dissenting).

The Missouri court en banc has unequivocally held that the language of an insurance policy must be viewed in the light of the meaning that would ordinarily be understood by the *lay person* who bought and paid for the policy. . . . The CGL Policy does not define 'damages.' If the insurer wished to use a technical legal meaning for that term which differed from the accepted dictionary definition, it should have explicitly done so.⁵⁷

The Fourth Circuit's decision, and the Eighth Circuit's en banc decision, also fail to address two principles essential to the panel opinion's original holding. First, the respective majorities ignore the proposition that governmental entities possess a legally protected interest in all real property within their borders. Instead, in *Maryland Casualty*, Judge Chapman merely writes that "'Damages,' as distinguished from claims for injunctive or restitutionary relief, includes 'only payments to third persons when those persons have a legal claim for damages'"⁵⁸ The original Eighth Circuit panel's conclusion that the federal and state governments' proprietary interests are sufficient to give rise to a legal claim for property damages would have included amounts awarded to governmental entities within this narrow view. Moreover, it is consistent with the statutory scheme of CERCLA, under which *all* governmental entities are considered "persons" for purposes of the statute's applicability.⁵⁹

Secondly, by focusing on the historical distinction between damages and equitable relief, the Fourth Circuit gives inadequate attention to the Eighth Circuit panel's conclusion that cleanup costs are a legitimate measure of property damages.⁶⁰ In *Maryland Casualty*, the court rejected this argument:

Damages is a form of substitutional redress which seeks to replace the loss in value with a sum of money. Resitution, conversely, is designed to reimburse a party for restoring the status quo. It might well cost far more to restore a contaminated marsh than it would to pay damages for its loss.⁶¹

The dissent in *Continental Insurance* correctly points out the inadequacy of this response, particularly in light of applicable Missouri law.⁶² Judge Heaney also notes that, under the facts of *Continental Insurance*, the costs of restoration would be markedly less than the diminution in real property value.⁶³

Since the fictional District Court is bound to follow *Continental Insurance Cos. v. Northeastern Pharmaceutical & Chemical Co.*, as decided by the

57. *Id.* at 988 (Heaney, J., dissenting) (emphasis in original) (citation omitted).

58. *Maryland Casualty*, 822 F.2d at 1352 (quoting *Aetna Casualty & Sur. v. Hanna*, 224 F.2d 499, 503 (5th Cir. 1955)).

59. *See* 42 U.S.C. § 9601(21) (1982).

60. *See* D. DOBBS, REMEDIES § 5.1, at 312 (1973). Missouri courts have adopted this view as well. *Jack L. Baker Cos. v. Pasley Mfg. & Distrib. Co.*, 413 S.W.2d 268, 273-74 (Mo. 1967); *Gulf, M. & O.R.R. v. Smith-Brennan Pile Co.*, 223 S.W.2d 100 (Mo. Ct. App. 1949).

61. *Maryland Casualty*, 822 F.2d at 1353.

62. *Continental Ins.*, 842 F.2d at 989-90 (Heaney, J., dissenting).

63. *Id.* at 989.

Court of Appeals en banc, XYZ will not be covered by any of the policies in place during the period of alleged contamination. Since the response costs do not represent damages compensating the plaintiffs in the underlying *United States v. XYZ* litigation, XYZ is not covered. All conditions precedent to coverage have been fulfilled except one - the CERCLA claim does not represent one for "damages."

This view is not without disagreement, however. Judges Heaney, Lay and Fagg dissented vigorously from the en banc opinion in *Continental Insurance*, distinguishing *Maryland Casualty* on the ground that it was decided under Maryland law, and contending that applicable Missouri law dictated that the term "damages" be read to include CERCLA cleanup costs.⁶⁴ Moreover, the Fourth Circuit's theory in *Maryland Casualty* has been rejected by a United States District Court in Delaware⁶⁵ and roundly criticized by another in Michigan.⁶⁶ In the latter case, the District Judge observed:

In this context the argument concerning the historical separation of damages and equity is not convincing and it seems to me that the insured ought to be able to rely on the common sense expectation that property damage within the meaning of the policy includes a claim which results in causing him to pay sums of money because his acts or omissions affected adversely the rights of third parties.⁶⁷

Thus, although the United States Supreme Court has denied certiorari in *Maryland Casualty*,⁶⁸ the final word on this issue may still be forthcoming. Interestingly, the United States government filed an amicus brief in support of the insured's position in *Continental Insurance*.⁶⁹

C. The Pollution Exclusion

The only policy defense left before our District Judge is the so-called "pollution exclusion."⁷⁰ Several courts have had occasion to construe the pollution exclusion in the hazardous waste context and, as with the previous policy defenses, the results have been mixed. It can be said, however, that a rough majority of courts have, for various reasons, held that the pollution exclusion does *not* defeat coverage.⁷¹

64. *Id.* 987-90.

65. *New Castle City v. Hartford Accident & Indem. Co.*, 673 F. Supp. 1359 (D. Del. 1987).

66. *United States Fidelity & Guar. Co. v. Thomas Solvent Co.*, No. K85-415, slip op. (W.D. Mich. Jan. 15, 1988).

67. *Id.*

68. 108 S. Ct. 703 (1988).

69. *Continental Ins.*, 842 F.2d at 984. Query whether the Solicitor General siding with CERCLA defendants is a modern day example of the old adage concerning "strange bedfellows."

70. For a history of the pollution exclusion, see Hunter, *The Pollution Exclusion in the CGL Insurance Policy*, 1986 ILL. L. REV. 897 (1986); R. LONG, *supra* note 6.

71. Note, *supra* note 7; *supra* note 4.

In contrast, representative of the minority, or non-coverage, view is *Great Lakes Container Corp. v. National Union Fire Insurance Co.*⁷² In *Great Lakes*, applying the "plain meaning" rule of contract construction,⁷³ the First Circuit Court of Appeals held that the language of the exclusion clearly and unambiguously precluded coverage for property damage resulting from disposal of hazardous waste where such disposal occurred in the regular course of the insured's business.⁷⁴

A recent case followed the minority rule of *Great Lakes*. In *Fischer & Porter Co. v. Liberty Mutual Insurance Co.*,⁷⁵ the district court held that cleanup costs incurred as a result of the insured's regular practice of disposing of trichlorethylene (TCE) were excluded from coverage by the terms of the standard CGL pollution exclusion.⁷⁶ Like the First Circuit, the Pennsylvania District Court found the terms of the exclusion unambiguous. The court then focused on the "sudden and accidental" exception to the exclusion and ruled that the *insured*, rather than the insurer, bore the burden of proving that the facts fell within the exception, because its applicability was an "issue of coverage."⁷⁷ The court found that the term "sudden," in the context of the exception, connoted an element of abruptness that was lacking when the release of TCE was the result of a regular and continuous disposal practice over an extended period of time.⁷⁸ By broadly construing the exclusion, and narrowly construing the exception, the district court held that the insured could not prove coverage under any set of facts.⁷⁹

This minority view would defeat coverage in most hazardous waste cleanup cases. Because it focuses on the "sudden" element of the exception, stating that it unambiguously requires the release to have been rapid, the minority view would not cover the vast majority of CERCLA § 107 cases; liability in the CERCLA context requires no abruptness of release.⁸⁰ In fact, CERCLA contemplates cleanup and cost recovery for *abandoned* sites, where the contamination has usually been the result of seepage, leaching or other latent conditions occurring over extended time periods.

It has been persuasively argued that the holdings in the minority view cases are result-oriented; that courts such as the First Circuit and the *Fischer* court would have ruled against the insured even in the absence of the pollution exclusion.⁸¹ The illegality of the insured's conduct, as in *Fischer*, may have

72. 727 F.2d 30 (1st Cir. 1984).

73. See *supra* note 18.

74. *Great Lakes*, 727 F.2d at 33. Note that the court also, perhaps erroneously, says "there is no occurrence within the meaning of the policy alleged." *Id.* at 33-34.

75. 656 F. Supp. 132 (E.D. Pa. 1986).

76. *Id.*

77. *Id.* at 134. Note that this procedural allocation goes against the traditional rule. See *supra* notes 20-22 and accompanying text.

78. *Fischer & Porter*, 656 F.2d at 134.

79. *Id.*

80. See *supra* note 10 for definition of "release."

81. Chesler, Rodburg & Smith, *supra* note 38, at 45.

also been a significant factor in denying coverage.⁸² Query whether minority view jurisdictions would be so quick to deny coverage in a case involving lawful disposal.

The majority, or pro-coverage, view uses several different theories to mitigate the harshness of the pollution exclusion. Some courts have noted a logical inconsistency between the language of the exclusion and that of the occurrence definition, noting that "liability insurance policies cover an occurrence, which by policy definition includes conditions continuing in nature, while the pollution exclusion clause excludes coverage unless the escape is sudden. Both propositions cannot be simultaneously true and the policy may be ambiguous."⁸³ Having found the requisite ambiguity, these courts invoke the *contra proferentum* canon of construction and ignore the exclusion.⁸⁴

Other majority view courts attempt to reconcile the exclusion's narrow "sudden and accidental" exception with its broad occurrence definition. In particular, a line of New York cases offers the theory that the word "sudden" does not necessarily connote "abruptness."⁸⁵ Rather, these cases conclude that the word sudden is subject to two possible definitions:

contrary to the insurers' assertion that "sudden" connotes "almost instantaneous," the word "sudden" is not defined in the policy and that the primary definition in a dictionary emphasizes unforeseeability with a secondary meaning emphasizing speed. . . . where a term in the pollution exclusion is susceptible to two reasonable interpretations, the one most favorable to the insured must be adopted.⁸⁶

This view has been criticized as a disguise for result-oriented judicial emasculatation of the pollution exclusion; "with this focus, courts have effectively read out of the exclusion any requirement of suddenness."⁸⁷ On the other hand, it may be just another effort at applying boilerplate policy language to unique factual situations involving peculiar considerations. For example, courts in the "New York line" have noted that "the word 'discharge'

82. Note that illegality was also an important factor in the decision of the *American States* court's holding that the release of hazardous substances was not an "occurrence." See *supra* notes 32-35 and accompanying text.

83. *United States v. Conservation Chem. Co.*, 653 F. Supp. 152, 204 (W.D. Mo. 1986) (citing *United Pac. Ins. Co. v. Van's Westlake Union, Inc.*, 34 Wash. Ct. App. 708, 664 P.2d 1262 (Ct. App. 1983)).

84. See, e.g., *Payne v. United States Fidelity & Guar. Co.*, 625 F. Supp. 1189 (S.D. Fla. 1985); *Buckeye Union Ins. Co. v. Liberty Solvent & Chem. Co.*, 17 Oh. App. 3d 127, 477 N.E.2d 1227 (Ct. App. 1984).

85. *National Grange Mut. Ins. Co. v. Continental Casualty Ins. Co.*, 650 F. Supp. 1404 (S.D.N.Y. 1986); *Niagara County v. Utica Mut. Ins. Co.*, 80 A.D.2d 415, 439 N.Y.S.2d 538 (1981); *Allstate Ins. Co. v. Klock Oil Co.*, 73 A.D.2d 486, 426 N.Y.S.2d 603 (1980).

86. *Conservation Chem.*, 653 F. Supp. at 203.

87. Note, *supra* note 7, at 763-64.

clearly refers to the original release of toxic chemicals However, the word 'dispersal' may refer to a secondary dissemination after the original release."⁸⁸ Given the propensity of some chemicals for rapid migration and the swift flow of groundwater in many aquifers, the requisite "abruptness" of release, while admittedly lacking from the initial deposit of the substances, would be present in later stages of contamination.⁸⁹

Some observers have noted that, absent the requirement of abruptness, the pollution exclusion becomes nothing more than a restatement of the occurrence definition, rendering the exclusion mere surplusage.⁹⁰ At least one court has so held.⁹¹ The insurers find this result unacceptable, given traditional judicial hesitance to construe contract provisions to be superfluous.⁹²

A rejoinder to this argument is that the very intent of the drafters of the pollution exclusion was to restate the occurrence definition, subject to a very narrow exception for intentional polluters.⁹³ Even some insurance industry attorneys have admitted that the exclusion was originally drafted to focus on the distinction between intentional and unintentional releases, rather than between gradual and nongradual ones, as insurers now claim.⁹⁴ If this is the context, it may be possible to reconcile the minority and majority view. If, in hazardous waste cleanup cases, the occurrence definition and the pollution exclusion mean the same thing, then an intentional or unlawful release, such as those in *American States* or *Fischer* would never be covered; the release would be either expected or intended and thus not an occurrence; or the release would not be sudden and accidental. On the other hand, where the disposal of hazardous substances were lawful and the contamination unintentional, as is presumably the case in the majority of CERCLA cleanups, both the occurrence definition and the exception to the pollution exclusion would be fulfilled.⁹⁵

Whatever basis the fictional district court uses in *Good Hands v. XYZ*, the chances are good that the pollution exclusion will not be invoked to preclude coverage. Although the Eighth Circuit expressly reserved judgment on

88. *Farm Family Mut. Ins. Co. v. Bagley*, 64 A.D.2d 1014, 409 N.Y.S.2d 294, 295-96 (1978) (quoted in *National Grange*, 650 F. Supp. at 1411).

89. This would also be consistent with the statutory definition of "release." See *supra* note 10.

90. See, e.g., Note, *supra* note 7, at 764 (citing *R. LONG*, *supra* note 6, app. at 59).

91. *Jackson Township Mun. Util. Auth. v. Hartford Accident & Indem. Co.*, 186 N.J. Super. 156, 451 A.2d 990 (Law Div. 1982).

92. See, e.g., *Conservation Chem.*, 653 F. Supp. at 202.

93. See, e.g., Hurwitz & Kohane, *Insurance Coverage for Environmental Accidents*, 50 INS. COUNS. J. 378, 378-79 (1983); McGeough, *The Applicability of Liability Insurance Coverage to Actions Involving Environmental Damage*, 1971 PROCEEDINGS OF INSURANCE, NEGLIGENCE, AND COMPENSATION LAW SECTION, ABA 312, 318-19.

94. Hurwitz & Kohane, *supra* note 93, at 381.

95. This dichotomy may explain the seemingly inconsistent results reached by the U.S. District Court, Eastern District of Michigan, discussed *supra* note 36 and in accompanying text.

the issue in *Continental Insurance*,⁹⁶ that court followed the majority view in a recent case. In *Benedictine Sisters v. St. Paul Fire & Marine Insurance Co.*,⁹⁷ the Eighth Circuit broadly construed the sudden and accidental exception to include the continuous discharge of soot from a smokestack over a period of several years.⁹⁸ Although not a CERCLA case, or even one involving hazardous substances, *Benedictine Sisters* may be a strong signal that the Eighth Circuit, following reasoning similar to that of the "New York line," will narrowly construe the pollution exclusion in hazardous substance cleanup cases.

VI. PUBLIC POLICY CONSIDERATIONS

Having concluded that the court in *Good Hands v. XYZ* will likely find in favor of insurers based upon the recent decisions of the Fourth and Eighth Circuits, another difficult question remains: given that standard CGL provisions *can* be read to preclude coverage for hazardous waste cleanups, *should* they be so construed? This public policy debate is the crucial, though oftentimes unspoken, rub of the reported cases.

A. The Deterrence Theory

The insurers argue that to provide coverage for such cleanups removes any incentive for hazardous waste generators and disposers to improve technology and prevent releases.⁹⁹ "Presumably, an insured who knows he will be covered by his liability policy even if he is grossly negligent in preventing releases of pollutants will be tempted to diminish his precautions, while enforcement of the [pollution] exclusion will encourage and maintain vigilance and reduce the risk of environmental injury."¹⁰⁰

In addition to the positive, deterrent, basis of this argument, it also strikes a negative, retributive chord. It seems to suggest that there is unfairness in placing the loss resulting from environmental contamination on the shoulders of the insurance industry, which took no part in causing the pollution; rather than the generators and disposers, whose industrial activities actually caused the releases of hazardous substances. If bankruptcy and financial ruin are the wages of sin, say the insurers, so be it.

These arguments subscribe to a number of logical fallacies, however.

96. *Continental Ins. Cos. v. Northeastern Pharmaceutical & Chem. Co.*, 811 F.2d at 1182-83 n.3 (8th Cir. 1987).

97. 815 F.2d 1209 (8th Cir. 1987).

98. *Id.*

99. See generally Adler & Broiles, *The Pollution Exclusion*, 19 LOYOLA OF L.A. L. REV. 1251 (1986); Rosenkrantz, *The Pollution Exclusion through the Looking Glass*, 74 GEORGETOWN L.J. 1237 (1986).

100. *Conservation Chem.*, 653 F. Supp. at 202 (citing *Waste Mgmt., Inc. v. Peerless Ins. Co.*, 315 N.C. 688, 340 S.E.2d 374 (1986)). Note, however, that Judge Wright rejected this notion, as well as the insurers' motions for summary judgment. *Id.*, at 204.

First, it is difficult to conceive how a potential lack of insurance coverage could affect deterrence when the harmful consequences of the conduct in question were unanticipated and unexpected at the time it was undertaken. That is, how can one be deterred from doing something when the potential consequences are unknown to him at the time he acts? On the other hand, if one knows of the harmful results, there is no coverage in any event; intentional pollution is already excluded, even under the majority, pro-coverage view of the pollution exclusion.¹⁰¹

Moreover, the idea of punishing insureds for their negligence by withholding coverage is inconsistent with the very purpose of liability coverage. No one argues that a negligent driver's coverage should be excluded when he causes an accident that results in serious personal injury and property damage. Indeed, the very purpose of liability insurance is to protect the insured against harmful future events which are unanticipated, and a "comprehensive general liability" policy, issued to industrial entities, seems to envisage coverage "for all manner of claims arising out of their activities."¹⁰²

B. *The Risk Management Theory*

Despite any perceived public interest in the deterrence of pollution, or retribution therefore, a strong argument has been made that insurers should bear the loss as a means of achieving economically efficient risk management.¹⁰³ The reasoning is that insurance companies are in the business of managing and controlling risks, and to that extent are better able to calculate the likelihood of potential financial exposure, ascertain financial needs in the event of such exposure, and adjust policy terms, conditions and premiums to reflect these factors.¹⁰⁴ Under this reasoning, *all* hazardous waste generators and disposers would ultimately bear the cost of cleanups, through higher cost, and less readily available, liability coverage. This would result in spreading the costs more efficiently and over a broader economic spectrum.¹⁰⁵ Such a view would seem to make better sense than placing the entire cost on those companies and individuals unfortunate enough to not to have dissolved or otherwise insulated themselves from liability before the government files suit; leaving them to the bankruptcy courts or poorhouses, while other polluters escape exposure completely.¹⁰⁶

101. For a discussion of the pollution exclusion, see *supra* notes 70-98 and accompanying text.

102. *Kissel v. Aetna Casualty & Sur. Co.*, 380 S.W.2d 497, 506 (Mo. Ct. App. 1964).

103. See Note, *Encouraging Safety Through Insurance-Based Incentives: Financial Responsibility for Hazardous Wastes*, 96 YALE L.J. 403 (1986).

104. See generally *id.*; Nixon, *RCRA: Financial Responsibility Provisions*, 36 AMERICAN U.L. REV. 133 (1986).

105. See Note, *supra* note 103.

106. See generally Note, *supra* note 103; Stewart, *The Role of Courts in Risk Management*, 16 ENVTL. REP. 10208 (1986).

This phenomenon may be occurring already. Since "to date [the] attempt by the insurance industry to address the area of hazardous waste disposal through the use of pollution exclusion clauses has been almost entirely unsuccessful,"¹⁰⁷ insurers have sought other means of risk management and control. Recently, insurers have promulgated new commercial liability policies greatly curtailing, if not eliminating, coverage for all manner of environmental damages.¹⁰⁸ For a substantially higher premium, a limited endorsement covering some such losses is available, but even these policies expressly exclude any coverage for cleanup costs.¹⁰⁹ These efforts are designed to compensate for, and prevent in the future, the huge financial loss, particularly in defense costs, associated with the "proliferation of delayed-manifestation claims."¹¹⁰

Certainly, public policy does not favor the financial destruction of XYZ, its officers, directors, and possibly shareholders.¹¹¹ Nor should public policy seek to punish people for past negligence when such retribution would serve to disappoint reasonable expectations arising under contracts. Finally, it is inconceivable that public policy should demand an uneven distribution of economic loss throughout a cost recovery system, which might undermine the very purpose of CERCLA: to secure cleanup of hazardous substances in the most efficient manner possible and at the lowest possible cost to taxpayers. Public policy supports insurance coverage for hazardous waste cleanup costs.

VII. CONCLUSION

The outlook for XYZ's defense of the declaratory judgment action is not good. The district judge, bound by the recent decisions of the United States Court of Appeals, Eighth Circuit, will likely grant the insurers' motions for summary judgment on the basis of policy defenses. This will be true despite the fact that XYZ can prove that the contamination at the Pleasant Valley site was unexpected and unintended, thus showing the requisite "occurrence," and further that the release of chemicals at the site resulted in soil and groundwater contamination during the policy periods, constituting compensable damage to property in which the United States has a cognizable interest. Even though the property damage was entirely fortuitous, and thus "sudden and accidental," none of the insurers' policies provide coverage for the response costs in the underlying lawsuit. Such a result is untenable in light of long-standing traditions of insurance law and modern policies underlying environmental legislation. Although there is certainly no consensus in the courts on

107. Note, *supra* note 7, at 765.

108. Fitzgerald, *The ISO's Commercial General Liability Policy*, 43 J. MO. BAR 383 (1987).

109. *Id.*

110. Mosher, *Insurance Limits of Liability and Defense Costs: A Coverage Analysis*, 43 J. MO. BAR 375 (1987).

111. All are potentially liable as "owners or operators." *United States v. Northeastern Pharmaceutical & Chem. Co.*, 579 F. Supp. 823 (W.D. Mo. 1984).

these issues, and further litigation is imminent, sound public policy supports liability insurance coverage for companies like XYZ.

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